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FISCAL IMPACT STATEMENT

LS 6806 | **NOTE PREPARED:** Feb 24, 2005
BILL NUMBER: HB 1669 | **BILL AMENDED:** Feb 24, 2005

SUBJECT: Enterprise Zone Incentives.

FIRST AUTHOR: Rep. Hinkle | **BILL STATUS:** CR Adopted - 1st House
FIRST SPONSOR:

FUNDS AFFECTED: X **GENERAL** | **IMPACT:** State & Local
X **DEDICATED**
FEDERAL

Summary of Legislation: (Amended) The bill establishes the Enterprise Zone Investment Deduction, which allows a taxpayer who makes a qualified investment to obtain a deduction against the assessed value of a taxpayer's Enterprise Zone property located in an Enterprise Zone. The bill also establishes the Enterprise Zone Personal Property Deduction, that provides a deduction against the assessed value of the taxpayer's personal property located in an Enterprise Zone to a maximum of $250,000. The bill allows a taxpayer to assign the Enterprise Zone Investment Cost Credit. It provides that trusts, estates, corporations, and pass through entities that make qualified investments in Enterprise Zone businesses may claim the Enterprise Zone Investment Cost Credit. (Current law allows only individuals to claim the credit, except in Vigo County where pass through entities are also eligible.)

Effective Date: (Amended) January 1, 2000 (retroactive); July1, 2005; January 1, 2006.

Explanation of State Expenditures: (Revised) *Department of State Revenue (DOR):* The DOR would incur some administrative expenses as a result of allowing taxpayers to transfer the Enterprise Zone (EZ) Investment Cost Credit (ICC). The bill requires the DOR to administer the tax credit transfer process and establish a reporting system for tax credit transfers. The DOR also may have to revise tax forms, instructions, and computer programs to deal with credit transfers. The DOR also is required to annually compile and report to the Indiana Economic Development Corporation (IEDC) information on the EZ Loan Interest Credit. The DOR's current level of resources should be sufficient to implement these responsibilities.

Enterprise Zone Fund: The bill would allow money in the Enterprise Zone Fund to be used to pay administrative expenses of Urban Enterprise Associations (UEAs). The UEAs are local nonprofit entities that operate the EZs. Currently, money in the Fund may be used to: (1) pay the expenses of administering the Fund; (2) pay nonrecurring administrative expenses of the EZ Program; and (3) provide grants to UEAs for brownfield remediation in EZs. The Fund is administered by the IEDC and contains revenue from the EZ business registration fee. Businesses receiving EZ incentives must pay a fee equal to 1% of the incentives obtained by the business if the incentives exceed $1,000 during the year. The FY 2004 balance in the Fund totaled $259,437, and the balance in the Fund as of February 23, 2005, was $314,657.

Explanation of State Revenues: (Revised) *EZ Investment Cost Credit (ICC):* The bill extends the ICC to corporations and pass through entities and allows a taxpayer who is entitled to claim the ICC to assign any portion of the credit to another taxpayer. The bill requires the taxpayer assigning the ICC to contribute 14% of the proceeds of the assignment to the Urban Enterprise Association for the EZ in which the taxpayer is located; and to reinvest the remaining proceeds in the taxpayer's EZ operations.

Over the years $2.9 M in credits have been approved. However, data is unavailable indicating the amount of this approved credit total that has been claimed by taxpayers against their tax liabilities. Assuming that currently unused credit amounts would eventually be utilized, allowing assignment of the ICC has no long-run fiscal impact. The change simply provides for more timely use of these outstanding credits already obtained by taxpayers.

Both changes, however, could potentially increase the certification of new credits in future years. Since data describing the investment behavior of EZ businesses is unavailable, the fiscal impact of new credit activity is indeterminable. The revenue impact depends on the extent to which the changes to the ICC encourage future equity investment in EZ businesses. Credits for investment encouraged by the ICC or the changes made by this bill presumably are not a revenue loss to the state. However, if the investment would have occurred in the absence of the ICC or the changes made by this bill, the net impact would be the total credits claimed by investors.

Background: Under current statute, the ICC may be claimed against the Adjusted Gross Income (AGI) Tax by individuals purchasing an ownership interest (an equity investment) in an EZ business. Current statute allows pass through entities investing in businesses in a Vigo County EZ to claim the ICC. The ICC is equal to a maximum of 30% of the equity investment. The credit percentage allowed (up to 30%) varies depending upon the type of investment, the type of business, and the number of jobs created. The credit is nonrefundable, but a taxpayer may carry over excess credits to subsequent taxable years. Revenue from the AGI Tax on corporations, the Financial Institutions Tax, and the Insurance Premiums Tax is distributed to the state General Fund. Eighty-six percent of the revenue from the AGI Tax on individuals is deposited in the state General Fund, and 14% of the revenue is deposited in the Property Tax Replacement Fund.

EZ Business Registration Fee: One percent of the incentive dollars obtained by taxpayers claiming EZ tax incentives could potentially flow to the IEDC through the EZ business registration fee. Businesses receiving EZ incentives must pay a fee equal to 1% of the incentives obtained by the business if the incentives exceed $1,000 during the year. The additional registration fees that could potentially be generated by the property tax deductions established in this bill are indeterminable.

Explanation of Local Expenditures:

Explanation of Local Revenues: (Revised) *Enterprise Zone (EZ) Investment Deduction:* This provision would allow the increase in assessed value (AV) from "qualified investment in real and/or personal property of an EZ business to be deducted for up to 10 years. If there is an increase in development in the EZs because of the deduction, the new real and personal property would, after no more than 10 years, be placed on the tax rolls. This could help spread the property tax burden and could possibly reduce some tax rates. However, assuming that the investment would have been made in the absence of the deduction, the deduction results in a delay of the shift of the property tax burden from all taxpayers to the owners of the new property until the property is placed on the tax rolls.

The deduction would apply to the remainder of: (1) the total AV of the taxpayer's EZ real and personal property on a particular assessment date **minus** (2) the total AV of the taxpayer's EZ real and personal property in the year prior to the year in which the qualified investment was made (defined as the "base year AV).

Under the bill, qualified investment would be any of the following expenditures relating to an EZ location on which a taxpayer's EZ business is located:

(1) The purchase of a building.
(2) The purchase of new manufacturing or production equipment.
(3) The purchase of new computers and related office equipment.
(4) Costs associated with the repair, rehabilitation, or modernization of an existing building and related improvements.
(5) Onsite infrastructure improvements.
(6) The construction of a new building.
(7) Costs associated with retooling existing machinery.

A taxpayer must apply to the county auditor to claim the deduction for a particular year. The county auditor would determine whether the taxpayer is eligible for the deduction.

Enterprise Zone (EZ) Personal Property Deduction: This provision would allow a deduction for tangible personal property located in EZs. The reduced valuations on EZ tangible personal property would shift part of the property tax burden from the taxpayers who own the personal property to all taxpayers in the form of an increased tax rate. Total local revenues, except for cumulative funds, would remain unchanged. The revenue for cumulative funds would be reduced by the product of the fund rate multiplied by the deduction amount applicable to that fund. The amount of the tax shift cannot be estimated.

The deduction would apply to tangible personal property that is located within an EZ on the assessment date. The deduction would be equal to the lesser of: (1) the AV of the EZ personal property; or (2) $250,000. A taxpayer must apply to the county auditor to claim the deduction for a particular year. The county auditor would submit the application to the municipal fiscal body containing the EZ personal property. If the fiscal body approves the application, the taxpayer is entitled to the deduction for the assessment year.

State Agencies Affected: Department of State Revenue, Indiana Economic Development Corporation, Department of Local Government Finance.

Local Agencies Affected: County auditors, fiscal bodies in municipalities with EZs..

Information Sources: Indiana Department of Commerce, Enterprise Zone Business Registration data.

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